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The emerging landscape of supply chain real estate - by Zain Jaffer

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Supply Chain

Material shortages, loss of labor, restrictions on global travel and bottlenecked production–it seems like a fatal equation. Far from thwarted by the COVID-19 recession, supply chain disruptions throughout the pandemic have strengthened the industrial and logistics sector. The supply chain process in full is undergoing mass re-consideration, a pandemic-prompted evaluation that is long overdue, and lasting changes in storage and distribution are guaranteed. As the sector continues to shape shift, all the while showing great resilience amid the global recession, certain changes have already cemented.

Virtual Demand: Already a massive agent of change, online sales have skyrocketed throughout the pandemic, making virtual demand a catalyst of activity and adaptation for the COVID-adjusted industrial real estate market. Studying e-commerce as a percent of total retail sales in the 10 countries with the highest retail output, Euromonitor predicts a rise from 17% in 2019 to 21% in 2021, and a jump to 39% by 2030.

Quarterly figures released by the U.S. Department of Commerce cited a national 30% raise in e-commerce sales between the first and second quarter of 2020, at the pandemic's inception. Further, findings from IBM's U.S. Retail Index make the claim due to the circumstances of COVID-19, the shift away from physical commerce toward digital shopping has been accelerated by approximately five years.

The Best Thing Since Sliced Bread: Garnering new demand in the e-commerce world are the grocery and beverage industries, with virtual sales having accelerated by 12% and 16% since the lockdown, respectively. The New York Times released an article in May citing several studies which found that more than a third of all Americans made their first online order for groceries during the month of April.

As for the direct beneficiaries of those orders, Instacart seems to be a crowd favorite. While the company wasn't an industry giant in the pre-COVID world, results from the Earnest Research market report show Instacart has seen the largest positive change in sales in the industry. Walmart maintains a relative 50% of online sales in grocery delivery. FreshDirect, a service that focuses largely on New York vendors, remains relatively steady without a notable spike in demand–the company spoke publicly about its inability to find healthy employees throughout the beginning of the lockdown.

'Just-In-Case' is Here To Stay: Aside from e-commerce and new online grocery sales, demand for storage is also spiking due to a surge in safety stock by retailers everywhere. Born from the inefficiencies of COVID-era supply, and cemented by erratic consumer behavior and the unforgettable panic of toilet paper shortages, nearly every retailer has chosen to increase their storage in stock. Considered a long term pivot more than a short term solution, this mass move away from lean-inventory strategies will drive demand for warehouses and land on which they can be built.

The Emerging Landscape of Supply Chain Real Estate: Demand remains steady in the industrial and logistics sector as supply chains stay afloat due to three major trends–an accelerated adoption of e-commerce, an exaggerated move toward virtual grocery and beverage sales, and the widespread adoption of increased safety inventory. And while demand is expected to stay high and consistent, value in the real estate market will differ between property types and market locations.

Perhaps the most important lesson learned by retailers this year is the importance of redundancy in their supply chain strategy. The supply chains reliant on Mainland China, already discouraged by trade tariffs and rising labor costs, experienced operation-ending bottlenecks. As a result, retailers have new interest for other parts of the global market. Whether retailers choose to completely uproot their operations or to add additional touchpoint for the purpose of redundancy–the “China Plus One” strategy–Asia, Europe, Mexico, and the U.S. can expect to house most of that newly diverged interest.

E-commerce is principally driving demand for big-box space, cold storage, and final mile warehouses near large population centers. A midyear outlook report from CRBE expects established markets near large population centers to suffer the lowest negative impact of the ensuing recession. The decentralization of the supply chain market is a compounding factor, increasing an already high absorption rate for Gateway logistics properties–real estate that has access to a major sea port and several metro areas within a one-day truck delivery.

New York, New York: In 2019, Prologis Research reported that Gateway facilities in Greater New York could access roughly $200 billion in income within only an hour, and $2.7 trillion within a one-day truck drive. Furthermore, city distribution properties in Greater New York were able to reach $400 billion within one-hour, and final mile warehouses in the same area had an income reach of roughly $550 billion.

COVID-inspired e-commerce is driving new need for final mile warehouses and near-consumer storage, especially e-commerce sales in the grocery and beverage industry. Safety inventory will only add to the need for space. As the industry continues to decentralize, it’s this kind of well-established, metropolitan-adjacent market that should see an uptick in demand–and at the very least, a lack of disruptions–throughout the economic fallout of COVID-19.

Suburban Demand: Secondary and tertiary suburban markets are more susceptible to the wavering demand of their local economies, and thus might reflect the downturn of the recession in its early stages. However, these are areas in which e-commerce interest is climbing at the same rate, and final mile warehouses will eventually see that same increase in demand. Any investor searching for longer-term yield opportunities might find great promise in the secondary and tertiary suburban industrial market.

Investors, retailers, and suppliers alike are witnessing a rapid re-imagination of supply chain practices. The sector remains strong, even as it shifts. E-commerce and safety inventory are shouldering the demand, while the need for redundancy is decentralizing the market and the draw toward big-box space and final mile warehouses are introducing new competition to the industry. While much remains in flux, the resilience of the logistics and industrial sector is strong, without a shadow of a COVID-19 doubt.

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